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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 94

UNITED STATES OF AMERICA,
Appellant,
vs.
EL PASO NATURAL GAS COMPANY, et al.,
Appellees.

On Appeal from the United States District Court for the District of Utah

BRIEF AMICUS CURIAE on Behalf of the State of California

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December 27, 1963.

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STATEMENT

This appeal is a sequel to *California v. Federal Power Commission*, 369 U.S. 482 (1962), wherein this Court held that the Federal Power Commission (Commission) exceeded its jurisdiction in approving an asset acquisition between El Paso Natural Gas Company (El Paso) and Pacific Northwest Pipeline Corporation (Pacific) at a time when such transaction was, upon complaint of the United States of America, charged to be in violation of Section 7 of the Clayton Act.[1]

1. 38 Stat. 731, as amended 64 Stat. 1125, 15 U.S.C. § 18.

Subsequent to this Court's decision, the Commission over objection by California issued El Paso a temporary authorization to continue operation of its Northwest Division (formerly Pacific).

On October 19, 1962, United States District Court Judge Willis W. Ritter verbally dismissed the antitrust suit. (*United States v. El Paso Natural Gas Co. and Pacific Northwest Pipeline Corp.*, U.S. District Court for the District of Utah, Civil No. 143-57.) This appeal followed.

INTRODUCTORY STATEMENT

California adopts the Jurisdictional Statement and those other portions of the brief of the United States of America, Appellant herein, setting forth the Proceedings Below, the Questions Presented and the Statutes Involved. Additionally, however, certain facts coming from *California v. Federal Power Commission, supra*, including the history and rationale of that case, are relevant to this appeal and will be recited.

The golden gas market which is California is the prize of this contest. The issue here is whether the increasing needs of this market shall be met by the one economically dominant supplier—El Paso. And pertinent then to such issue are El Paso's rise to dominance; the aborted efforts of Pacific to function, and the reality and possibility of past and future competition; the efficiency of the Natural Gas Act[2] as a control device over pipeline monopoly. The facts herein must therefore be read in light of the purpose of the Clayton Act and the Natural Gas Act together.

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2. Act of June 21, 1938, c. 556, 52 Stat. 821-833, 15 U.S.C. §717-717w.

BACKGROUND OF THE MERGER

The Pacific Northwest Pipeline Corporation.

Pacific was incorporated under the laws of Delaware on June 2, 1949. Thereafter, commencing in 1950, a series of applications was filed with the Federal Power Commission under Section 7(e) of the Natural Gas Act,[3] seeking authority and related rights to construct an interstate natural gas pipeline. The broad authority requested was for "the construction, acquisition, and operation*** of a pipeline system for the interstate transportation of natural gas from a point or points in the States of New Mexico, Texas, and Colorado to points in the States of Utah, Washington, and Oregon ***".

On June 18, 1954, Pacific was granted a certificate. *Re: Northwest Natural Gas Company,* Opinion No. 271, June 18, 1954, 13 FPC 221. As the Opinion of the Commission stated at page 235:

> "The Pacific Northwest is the one remaining large area of this country with a great need for natural gas but which is still without this highly desirable fuel and raw material. It is a section where great industrial expansion has occurred and is still in progress and one which has played and continues to occupy a very important role in the national defense. The record amply demonstrates that it has a real desire and need for natural gas."

The Decision in discussing the future of Pacific stated this at page 232:

> "The economic feasibility of the Pacific project has been challenged. From a review of all the evidence we believe that Pacific's estimates are reasonable *and that its project is economically feasible. Under the rates*

3. 52 Stat. 824, 15 U.S.C. § 717f (e).

proposed to be charged they can secure the estimated volumes and such rates will produce revenues adequate to cover operating expenses and taxes with sufficient return to insure the necessary financing." (Emphasis supplied.)

The El Paso Natural Gas Company.

El Paso was originally organized in 1928 to bring gas to the area in and around El Paso, Texas. In 1946 El Paso received authorization to deliver gas to the Southern California Gas Company and the Southern Counties Gas Company of California. In 1949 El Paso was authorized to deliver gas to the Pacific Gas and Electric Company of California. El Paso then became the sole out-of-state supplier of natural gas to California.

El Paso has experienced phenomenal growth. Initially in 1929 its pipeline was 200 miles in length with a delivery capacity of 36,000,000 cubic feet (R. 359). In 1961 its system was 18,812 miles of main and lateral pipelines with a certificated delivery capacity of approximately 2.7 billion cubic feet of gas per day (R. 359).

Today El Paso is one of the largest nonfinancial corporations in the United States. At the end of 1957 it ranked 29th in size and was the largest of the natural gas companies. It controls and has interests in natural gas properties extending from western Canada to the Republic of Mexico, and from Oklahoma to the California border. El Paso has invested more than $1,600,000,000 in the facilities that comprise its system. Some has gone to supply the markets it serves in Texas, New Mexico and Arizona. It is estimated that a full 80 per cent of its investment has gone into serving the California market.

The California Market Area.

The dependence of California upon natural gas as a fuel is unique among the states. California does not possess coal deposits sufficient for energy requirements. It is dependent upon natural gas for its energy needs and approximately three quarters of the natural gas utilized in California comes from out-of-state sources. Ninety per cent of all homes in California are heated by natural gas and California industry depends upon natural gas as a fuel. In California the percentage of total energy provided by natural gas is substantially greater than for the nation as a whole.

During 1962, California gas distributing utilities purchased over 745,000,000,000 cubic feet of natural gas at a cost somewhat in excess of $266,850,000. California takes in excess of ten per cent of all of the natural gas moving in interstate commerce throughout the United States and exceeds the volume of gas imported by any other state.

The interest of California in this proceeding is evident. More than 80 per cent of the customers of El Paso before merger resided in the State of California and California ratepayers bear most of the costs of service of El Paso.[4]

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4. "The largest volumes of the Company's gas sales are made under long-term contracts with Southern California Gas Company and Southern Counties Gas Company of California (the 'Southern California Companies'), which through their distribution systems supply natural gas for most of the domestic, commercial and gas requirements of Southern California, including Los Angeles, and with Pacific Gas and Electric Company ('Pacific'), which distributes and sells electric energy and natural gas throughout a large part of central and northern California, including the San Francisco Bay area. The other customers include Nevada Natural Gas Pipe Line Company, which serves Las Vegas, Nevada, and environs, and 64 customers in west Texas, New Mexico and Arizona, six of which purchase gas at field delivery points for use in carbon black plants and miscellaneous field purposes. The other 58 customers include utility companies and municipalities purchasing gas for distribution to approximately 385,000 gas customers, utility companies purchasing gas for use in the generation of electric power, copper

California, alone, consumes more natural gas than the Middle Atlantic states combined, more than half as much as the highly industrialized, thickly populated East North-Central states of Illinois, Indiana, Michigan, Ohio and Wisconsin, and as much as the seven states that make up the West North-Central area. Out-of-state deliveries to California averaged three billion cubic feet per day in 1961. At a price of slightly more than thirty cents per thousand cubic feet (Mcf), this business was worth then about $1,000,000 per day.

COMPETITION FOR THE CALIFORNIA MARKET

Pacific's Planned Entry into the California Market.

The Pacific pipeline, as authorized and as constructed, was designed to serve the states of the Pacific Northwest and the Rocky Mountain area. The system map (Exh. GX 52 R. 407-408) discloses a proximity and, accordingly, an ability to furnish natural gas to California and in competition with El Paso. Pacific was conceived upon the ultimate hope and expectation of transmitting Canadian gas to California and to eastern markets. Ray Fish, organizer of Pacific and former chairman of its board of directors, testified that in early 1956 he had explored the possibility of serving the Chicago market. (R. 787). In May of 1956, Mr. Fish entered into preliminary negotiations with the Southern California Edison Company (Edison), a large California electric util-

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mining and other mining companies, and various other industrial consumers. Of the total revenues to the Company from the sales of gas during the twelve months ending April 30, 1956, revenues from gas sales to the Southern California Companies and Pacific amounted to 37.65% and 36.50%, respectively, while the revenues from gas sales to the five largest of the above-mentioned 64 customers were 6.69%, 2.69%, 2.07%, 2.03% and 1.23%, respectively." (R. 280-281).

ity, with a view to transporting and selling Canadian gas to Edison (R. 755-758). Speaking of a possible pipeline to California, Fish further stated:

"Why, we most certainly could have financed a line because any line that we would have undertaken would have had to have been economically feasible. Therefore, we could have financed it.

"I have never entered into a contract that I have not or could not finance.

"Mr. Kurtz: Yes. And even when you were negotiating for the sale of that gas to the California markets there was no doubt in your mind that you could finance that pipeline, was there?

"The Witness: No, sir, because the type of contract I would have with my customer companies would be such on which I could finance.

"Mr. Kurtz: That is right.

"And did you at this time also discuss with your finance people your proposals to build lines to the California market?

"The Witness: I believe our main investment house knew about it—Mr. Kiernan, of White, Weld, who is now a special partner of it.

"I mean, I think we discussed it casually with him.

"Mr. Kurtz: And did Mr. Kiernan at any time discourage you on the grounds that you could not finance such a project?

"The Witness: Not that I remember. In fact, there was not any doubt in my mind. It might have been hard to do, but again, it would be based on making a suitable contract with the market company that would make a line economically feasible, and then you can finance it." (R. 789-790)

Illustrative of Pacific's opinion as to the California market is the statement contained in the minutes of the special meeting of the board of directors of Pacific held on Febru-

ary 22, 1956, wherein these comments concerning a merger with El Paso were noted:

> "A full discussion ensued, in which the various advantages and disadvantages of such a merger were discussed***. Such a hearing would involve an expenditure of large amounts of time and money at a critical period in the corporation's existence; i.e., during the period it was organizing its personnel and preparing for the commencement of gas sales. It was suggested that preliminary investigation had disclosed that *there would be considerable opposition on the part of the Federal Power Commission to such a merger. Opposition had also been indicated from the market areas of California and the Pacific Northwest. It was felt that the corporation should not incur opposition from its markets at the present time, when the corporation is greatly dependent upon their support.*" (Emphasis supplied) (R. 332-333)

Pacific, it is to be noted, placed California in its market area.

The Negotiations to Enter the California Market.

In May of 1956, negotiations commenced between Ray Fish, of Pacific, and Harold Quinton, of the Southern California Edison Company. Quinton was interested in obtaining a direct supply of gas for Edison, and negotiations seeking to furnish 300,000,000 cubic feet of Canadian gas to Edison were undertaken. Cost estimates were made, and on July 30, 1956 a preliminary letter agreement was entered into between Pacific and Edison, providing for delivery of 300,000,000 cubic feet per day at the Oregon-California border, beginning November 1, 1959 (R. 755-758).

Initially, Edison would have been unable to utilize the entire 300,000,000 cubic feet of gas, and it became apparent

that the cooperation of the California distributing companies would be required to provide an initial market. Quinton solicited the Southern California Gas Companies (Pacific Lighting group) and the Pacific Gas and Electric Company, the two largest California gas distributors, and El Paso's largest customers. In August of 1956, both companies rejected the proposal. It may be fairly inferred that El Paso made known to the California gas distributing utilities its opposition to such a project (R. 568-570).

El Paso's Suppression of Pacific's Competition.

Paul Kayser, president of El Paso, aware of such efforts, flew to California in the fall of 1956 and discussed with Harold Quinton of Southern California Edison Company the offer of Pacific to serve Edison. Kayser advised Quinton that any arrangements with Fish *"would not be in the public interest."* (Emphasis supplied.) Kayser told Quinton that he would oppose any purchase which did not take into account the fact that Edison was a customer of the Pacific Lighting Group gas companies. The project was not consummated!

The fact of actual competition between Pacific and El Paso is demonstrated by the record. Pacific was conceived by its promoters as being a future supplier to the California gas market. Pacific took specific action to accomplish projects leading to gas sales to California public utilities. The fact of competition furnished by a separate and an independent Pacific was freely conceded by El Paso.

As stated in the record by Paul Kayser, president of El Paso:

> "Q. Now, as I understand it, prior to your acquisition of the stock of Pacific, you were in competition—there was competition between Pacific Northwest and El Paso for certain markets in the State of California.

"A. That is right. We were both trying to sell specifically Pacific Gas and Electric Company quantities of gas." (R. 471)

Other Competitive Activity.

As a separate, independent corporation, Pacific was caught up in a flurry of competition with El Paso. The record is replete with instances of El Paso's economic power, coming from a position of dominance as California's sole out-of-state gas supplier, being asserted in contests with Pacific.

For example, one of the pipeline corporations referred to in the record, West Coast Transmission, Ltd. (West Coast) had, on June 16, 1952, obtained authority from the Province of Albert to export gas into the United States from western Canada. Negotiations were conducted between West Coast and Pacific, leading ultimately to a contract between the two corporations, whereby West Coast would deliver to the border and Pacific would pick up initial deliveries of 200,000 Mcf per day for ultimate delivery to the California market. (R. 308-316) El Paso asserted itself into this arrangement and secured an agreement with West Coast and Pacific. The construction placed upon such agreement, is outlined in Pacific's letter to stockholders of December 22, 1954.

"This tri-party deal will benefit all concerned. It will give Westcoast what they have been fighting for—a pipeline. It will mean that Pacific will expand its facilities, be a larger company, will protect its market from future competition by a Canadian pipeline and it caused the dismissal of the law suit of Westcoast against Pacific's present certificate. *It means that El Paso's California market will be protected against future competition****." (Emphasis supplied.) (R. 800)

In short, by the agreements reached, El Paso sought to quell the competition of Canadian gas from Pacific and, indeed, the last paragraph of the letter referred to above makes reference to the tri-party agreement—in these terms:

> "• • • we believe that the 'treaty' which we have entered into will solve the major problems which have been confronting us."

Despite this "treaty" arrangement, Pacific made continued efforts to reach the California market, and Ray Fish characterized Pacific's ability to furnish gas to the California market in these terms:

> "I don't see how any pipeline to California markets from Canada can go through Pacific's territory and get to any California market cheaper than what Pacific can render that service for in the Northwest area."

Up until the time of the stock transfer by the stockholders of Pacific to El Paso, Pacific made efforts to sell gas to California.

Competition for Gas Supplies.

Control of a reliable gas supply is, of course, essential to a gas transmission company. There are many instances in which the economic strength of El Paso asserted itself in competition for critical gas supplies. This had the effect of both keeping these reserves from competitors and preventing these competitors from entering El Paso's California market area.

In the Aneth Field of the Southwest, the promoters of the Transwestern Pipeline Corporation sought sufficient gas supplies to justify the granting of a certificate to construct a pipeline to California. El Paso, by bidding away from Transwestern the Aneth supply, reduced and made

more difficult the reality of Transwestern's obtaining a certificate (*El Paso Natural Gas Co.*, 27 FPC 369, 377, 1960).

Tennessee Gas Transmission manifested a desire to build a pipeline to California. El Paso, by bidding for gas reserves in the Big Piney area of the Rocky Mountains, obtained a supply of gas therein at a contract price of 18½ cents, thus establishing a new high for gas purchased in that area. Any potential competitor seeking to construct a pipeline to California, as did Tennessee Gas Transmission, was handicapped, even precluded from obtaining a sufficient gas supply to support a certificate showing, by having the gas bid away from it by El Paso at new high area prices *(California v. Federal Power Comm.* 369 U.S. 482 (1962), R. 334-336).

El Paso's economic power appears in opposition to the then only contemplated Pacific Gas Transmission Company pipeline to run from western Canada to northern California. Pacific Gas Transmission, in order to obtain a certificate, was required to obtain and to show sufficient gas reserves to support such project. Asked whether El Paso would oppose the Pacific Gas Transmission line, this reply was given:

> "The Witness: Oh no. I would say that as to a given piece of gas in Canada—and this has already happened—where Pacific wants to buy it, Pacific Gas and Electric Company wants to buy it, and I need to buy it for the needs of my customers, I *am going to compete to buy.*" (Emphasis supplied.)

The bidding of gas reserves to new price highs only served as an upward push upon the price of a vital commodity, at an ever increasing, burdensome and unnecessary cost to ultimate consumers. The ability to make and to meet new, historic high prices is closely related to the economic power of El Paso.

EVENTS LEADING UP TO THE MERGER

Background of the Stock Acquisition.

Pacific, formed in 1949, filed its first applications with the Federal Power Commission in June of 1950. Its initial certificate authority was granted on June 18, 1954, and in April, 1955 Pacific's initial financing was complete. (R. 765)

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5. In connection with the management of Pacific prior to stock acquisition, the record shows the following holdings of Pacific common stock by Pacific's management:

Directors and Officers of Pacific	Common Stock of Pacific
Clyde H. Alexander, Director	715
Arthur B. Allyne, Vice President	500
J. M. Clark, Vice President	2,000
Ray C. Fish, Director and Chairman of the Board	118,892
Alfred C. Glassell, Jr., Director	98,212
Robert R. Herring, Director	20,000
Allen B. Hyatt, Vice President	100
Norman V. Kinsey, Director	25,000
Leon M. Payne, Director, Vice President and Secretary	15,045
Franz Schneider, Director	19,157
Charles K. Schwartz, Director	5,157
Stuart F. Silloway, Director and President	2,100①
C. A. Watson, Treasurer and Assistant Secretary	700
C. R. Williams, Director and Vice Chairman of the Board	52,599

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① In addition Mr. Silloway is entitled under a subscription agreement entered into with Pacific on October 9, 1956 to purchase from Pacific 30,000 shares of its Common Stock at $31 per share. Mr. Silloway also has a stock option for the purchase of 30,000 shares of Common Stock of Pacific, exercisable 6,000 shares annually on or after June 15 of each year from 1957 to 1961 and terminating as to any unexercised portion on July 15, 1961, at the option price of $27.79 per share. Discussions are presently under way between the Company and Mr. Silloway contemplating an arrangement whereby if the proposed exchange offer is consummated Mr. Silloway may be afforded an opportunity to exchange for shares of Common Stock of the Company, on a ratio no more favorable to Mr. Silloway than the exchange offer, any shares of Common Stock of Pacific he may acquire as a result of the exercise of his said stock option. (See *California v. F.P.C.*, 369 US 482, R 660)

In June of 1955 construction of the Pacific pipeline commenced and in 1955 offers by way of merger were made from El Paso to Pacific. The initial offers were rejected, but ultimately the offer which was accepted was so attractive that Pacific surrendered its ownership to El Paso.

Pacific commenced test deliveries to certain customers in August of 1956.

As hereinbefore related, during most of the corporate history of Pacific it made real efforts to enter the California market, as well as other areas in which it could furnish competition to El Paso. As previously related, Pacific attempted to secure long-term gas purchase contracts with California gas and electric distributing utilities, and in August of 1956 Paul Kayser, president of El Paso, learning of such negotiations, persuaded the California utilities to terminate negotiations with Pacific.

The prospectus of July 31, 1956 filed with the Securities and Exchange Commission by El Paso is a persuasive document in support of the stock acquisition. The prospectus recites in detail the business of each corporation, sets forth the terms of the stock exchange offer, and states:

> "Operation of Pacific after the Exchange Offer.
>
> If the exchange offer is successfully consummated, it is expected that Pacific will continue to be operated as a separate corporation, and the management of the company has no present intent of merging Pacific into the company or having the company acquire Pacific's assets."

The prospectus also discussed the application of the antitrust laws to the proposed acquisition of the common stock of Pacific and stated:

> "• • • (T)he antitrust questions raised have no controlling precedent and are original, significant and

difficult ones which may require extensive hearings, proceedings, and examination and cross-examination of witnesses and experts to resolve. Counsel concludes that while the matter is not entirely free from doubt, it is their opinion that the proposed transaction is not in violation of the antitrust laws presently in effect as so far construed by the courts. The opinion states that it is rendered on the assumption that after full investigation, the purpose of the transaction would continue to prove to be as previously indicated * * *."

On November 8, 1956 El Paso entered into a stock exchange agreement with Pacific, and by May 1, 1957 El Paso had acquired 99.8 per cent of the outstanding stock of Pacific.

On December 31, 1956 the Securities and Exchange Commission wrote a letter to El Paso as to the stock acquisition and possible violation of the antitrust laws. In response thereto El Paso stated that on November 15, 1956, Paul Kayser, president of El Paso, and Arthur Dean, of Sullivan and Cromwell, attorney for El Paso, met with the Attorney General of the United States and members of his staff and submitted certain information to them. On the same day—November 15, 1956—Kayser had a conference with the Federal Power Commission.

The Stock Acquisition and the Price Paid.

In 1957, Pacific's records showed a loss of $2,067,000. Moreover, in order to merge, Pacific's bonds would have to be called. El Paso proposed to loan Pacific for this purpose the requisite $23,252,000. Pacific's immediate prospects of earning a fair return were not good.

Nonetheless, in order to acquire control of Pacific, El Paso issued five million of its shares. The dividend require-

ment on these shares was $1.30 each, or a total dividend requirement of $6,794,974. Pacific could not assist in meeting this requirement.

El Paso considered that it was offering common stock having a pro forma market value of approximately $151,800,000 for Pacific's common.

On the basis of market quotations of January 2, 1957, which, of course, reflects El Paso's offer, Pacific's common had a market value of approximately $93,400,000. At this same time Pacific's common had a book value of approximately $29,770,131. Therefore, El Paso paid $132,029,869 for Pacific over book value, and in excess of $58,400,000 over market value. This acquisition had the effect of diluting El Paso's earnings available to its common stockholders.

The Management of Pacific After Stock Acquisition.

When the stock exchange offer was completed by May 1, 1957, El Paso had acquired 99.8 per cent of the outstanding common stock of Pacific. As a result of stock acquisition, El Paso took over the management and control of Pacific, and in its first initial and complete year of operation as a natural gas pipeline corporation Pacific was managed, controlled, and directed as to all of its policies and decisions— whether for profit or loss—by El Paso.[6]

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6. THE COMMON DIRECTORATE.
Upon stock acquisition of Pacific, these officers of El Paso and directors thereof became officers of Pacific and directors thereof.

	El Paso Management	Pacific Management
Paul Kayser	Director and President	Chairman of the Board and Director
Howard Boyd	Director, Vice President and Assistant General Counsel	Director and Vice-Chairman of the Board

Operating Experience of Pacific.

Pacific placed its initial facilities in operation on January 1, 1957, operating a natural gas transmission system consisting of approximately 2,125 miles of main and lateral pipelines, extending in a general northwesterly direction from the San Juan Basin in New Mexico through the States of Colorado, Utah, Wyoming, Idaho, and Washington to a terminus at the international boundary between the United States and Canada.

Pacific never operated as a separate, independent pipeline corporation. The timing of the stock exchange offer, its acceptance and completion placed Pacific under the control of the management of El Paso.

System Costs Not Covered by Revenues.

The record shows that Pacific, in operation as a subsidiary corporation owned, controlled, and dominated by El Paso, sold natural gas to other pipeline companies. These companies were Mountain Fuel Supply, Colorado Interstate Gas Company, and El Paso Natural Gas Company. Pacific

A. R. Grambling	Director	Director
Frank Liddell	Director and General Counsel	Director
D. H. Tucker	Director and Vice President	Director
H. F. Steen	Director, Vice President and General Superintendent	Director
Lindsay Bradford	Director	Director
Fred T. Wagner	Director, Vice President, Associate General Counsel	Director
C. L. Perkins	Vice President and General Manager and Director	Director
Arnold R. La Force	Financial Vice President	Director

did not recover the full cost of service for gas delivered to the other pipeline companies.

Undercharges to Colorado Interstate and Mountain Fuel Supply for the year 1958 were $5,478,675, and the amounts for each year through 1964, were $32,993,307. These include the undercharges to El Paso commencing in the year 1960.

No reason is shown why Pacific should not recover the full cost of service for gas sales to other pipeline companies.

The Pacific annual report to stockholders for 1957 discloses a revenue deficiency approximating $14,000,000 and a net loss of $367,005 for the year ended December 31, 1957, the first year of operation under the control of El Paso Natural Gas Company. (R. 337-339)

The Decision to Merge.

Pacific operated as a separate pipeline corporation, but a subsidiary of El Paso, from January 1, 1957. On July 22, 1957, the United States of America, by complaint filed in the United States District Court for Utah, Central Division, charged that the purchase of Pacific stock by El Paso was a lessening of competition tending toward monopoly, in violation of Section 7 of the Clayton Act.

In order to avoid the possible consequences of the anti-trust action, as the Commission found, on August 7, 1957 El Paso and Pacific filed their respective applications with the Federal Power Commission, seeking administrative approval under the Natural Gas Act for the acquisition by El Paso of the assets of Pacific.

Summary of Events.

Dates	Events
June 28, 1950	Pacific files its first application with FPC.
June 18, 1954	Pacific granted a certificate as requested.
1955	El Paso negotiates for acquisition of Pacific.
May, 1956	Pacific negotiates to sell gas to California Utilities.
August, 1956	Kayser of El Paso persuades California gas utilities such arrangements with Pacific "would not be in the public interest."
July, 1956	El Paso prospectus sets forth terms of stock exchange offer and advises that Pacific will operate as a separate corporation.
November 8, 1956	Pacific and El Paso stockholders agree upon terms of the stock exchange offer.
November 15, 1956	Kayser and Arthur Dean of El Paso meet with the Attorney General of the United States concerning antitrust violations; Kayser and Dean meet with the Federal Power Commission.
December 31, 1956	The SEC inquires by letter as to possible violations of the antitrust laws because of the stock acquisition.
January 1, 1957	Pacific becomes operational.
July 22, 1957	The United States Attorney General commenced an action against El Paso and Pacific under Section 7 of the Clayton Act (Act of Oct. 15, 1914, c. 323, § 7, 38 Stats. 731; as amended Dec. 29, 1950, c. 1184, 64 Stats. 1125; 15 U.S.C. § 18), alleging that by its purchase of Pacific stock El Paso was lessening competition and tending to create a monopoly (*United States v. El Paso Natural Gas Company and Pacific Northwest Pipeline Corporation*, Civil Action No. 143-57 U.S. D.C. for Utah, Central Division).
August 7, 1957	El Paso and Pacific filed application with the Federal Power Commission seeking approval and authority for the acquisition by El Paso by merger of all of the facilities of Pacific.

SUMMARY OF ARGUMENT.

Application of the Clayton Act to this merger is required in the public interest. The Natural Gas Act does not give to the Federal Power Commission those powers needed to control and to regulate completely a pipeline such as El Paso. It is evident that the conclusion reached by the Trial Court is predicated, in part, upon the notion that a natural gas company cannot offend monopoly statutes since it is subject to regulation. The record is clear herein as to past instances of unlawful competitive activity and it is critical to the economic welfare of the West that the monopoly power created by this merger be set aside. The gas needs of the West and of California are best served through regulated suppliers exposed to those challenges, incentives and restraints which only competition offers.

ARGUMENT

The Natural Gas Act Does Not Intend a Monopoly.

The purpose of the Natural Gas Act is plain. As this Court has frequently stated the primary aim of the Act is "to protect consumers against exploitation at the hands of natural gas companies." *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 611 (1944); *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672, 685 (1954).

This purpose was reaffirmed in *Sunray Mid-Continent Oil Co. v. Federal Power Commission*, 364 U.S. 137, 147 (1960), and rephrased in *Atlantic Refining Co. v. Public Service Commission of the State of New York* (CATCO), 360 U.S. 378, 388 (1959): "The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges." See also *Federal Power Commission v. Transcontinental Gas Pipe Line Corp.*, 365 U.S. 1, 19 (1960).

Since exploitation is prohibited by law and is therefore to be prevented, realism compels a look at those situations which tend to promote and permit exploitation as against those which tend to reduce it. It is patent that exploitation is best realized from a monopoly position. Indeed the frequent and almost inevitable exploitation which arises under the deficiencies of the Natural Gas Act, even when suspected and ultimately known, is ever long in the proving and never completely cured. In *Federal Power Commission v. Tennessee Gas Transmission Co.*, 371 U.S. 145 (1962), this Court affirmed the Commission's power to order immediate refunds. It also recognized that even interim relief falls short. This Court stated, at pages 154-155:

> "Faced with the finding that the rate of return was excessive the Commission acted properly within its statutory power in issuing the interim order of reduction since the purpose of the Act is 'to afford consumers a complete, permanent and effective bond of protection from excessive rate and charges. . . .' *Id.*, at p. 388. To do otherwise would have permitted Tennessee Gas to collect the illegal rate for an additional 18 months at a cost of over $16,500,000 to consumers. *True, the exaction would have been subject to refund but experience has shown this to be somewhat illusory in view of the trickling down process necessary to be followed, the incidental cost of which is often borne by the consumer, and in view of the transient nature of our society which often prevents refunds from reaching those to whom they are due.* (Emphasis supplied).

The statutory wall which Congress has erected against exploitation gives weight to the argument that Congress did not intend economic dominance or monopoly in this field. Prior to the enactment of the Natural Gas Act fifty-

six per cent of all natural gas transmitted in interstate commerce was controlled by four holding companies; eighty-one per cent of the transmission was controlled by fifteen companies.[7] Congress was aware of this situation and one of the evils which the Natural Gas Act sought to control was dominance of the industry by the few. Congress intended to protect the public from the evils of monopoly by preserving free and unfettered competition as the rule of trade. *Northern Pacific Railroad Co. v. United States*, 356 U.S. 1 (1958).

The Natural Gas Act is direct and plain to this point stating in Section 7(g)[8]: "Nothing contained in this section shall be construed as a limitation upon the power of the Commission to grant certificates of public convenience and necessity for service of an area already being served by another natural-gas company." See *Panhandle Eastern Pipe Line Co. v. Federal Power Commission*, 169 F 2d 881 (D.C. Cir. 1948).

In *City of Pittsburgh v. Federal Power Commission*, 237 F.2d 741 (D.C. Cir. 1956), the court said:

> "The Commission, while it 'has no power to enforce the Sherman Act • • • [and] cannot decide definitely whether the transaction contemplated constitutes • • • an attempt to monopolize which is forbidden by the Act • • •' nevertheless 'cannot, without more, ignore the [Act] • • •'
>
> "Although the Commission has no power to enjoin conduct as illegal under the Sherman Act or even to declare such illegality, it certainly has the right to consider a congressional expression of fundamental natural policy as bearing upon the question whether a particular certificate is required by the public convenience and necessity."

7. S. Doc. No. 29, Part 84-A, 70th Cong., 1st Sess.

8. 52 Stat. 825, 15 U.S.C. § 717f(g).

The Natural Gas Act forbids exploitation. It forbids a grant of economic power which furthers monopoly and leads to exploitation. The purpose of the Natural Gas Act and the national policy against monopoly cannot be avoided in the name of regulation (*California v. Federal Power Commission, supra*). Nor is the national policy against monopoly to be thwarted by a loose construction of the Clayton Act as the trial court indulged in here. The lower court acted upon the unsophisticated notion that the Natural Gas Act permits undue economic dominance and in some unspecified manner equips the Commission to control it.

The Natural Gas Act is not an Effective Instrument for Monopoly Control.

The usual argument encountered to justify pipeline monopoly is that it is subject to regulation. The theory goes that such monopoly will not then be attended by the usual evil consequences. Such is not the case.

The Natural Gas Act as a control device has inherent deficiencies. Its history has demonstrated its inadequacy to meet the needs of consumers and the challenges of regulation. Initially it is important to note that natural gas companies are not public utilities. All of those public obligations and all of those controls which attach to public utilities do not obtain as to a natural gas company. A natural gas pipeline corporation is under no obligation to expand or to serve new markets; nowhere in the Natural Gas Act is the Federal Power Commission given the power to compel service. Decisions relating to service of the vital commodity, natural gas, rest with management.

Most regulatory commissions have power to control the capital costs of public utilities. By way of example, the

Public Utilities Code of the State of California specifically provides:

"Section 816.

"The power of public utilities to issue stocks and stock certificates or other evidence of interest or ownership and bonds, notes, and other evidences of indebtedness and to create liens on their property situated within this State is a special privilege, the right of supervision, regulation, restriction, and control of which is vested in the State, and such power shall be exercised as provided by law under such rules as the commission prescribed."

Other regulatory commissions have like authority.

The relevance of security regulation to the function of a commission is well stated by Barnes in *The Economics of Public Utility Regulation, G. S. Crofts & Co., 1947*, at page 683:

"The modern attitude rests on the conviction that the control of security issues and capitalization constitutes a cornerstone of effective public utility regulation. The control of security issues is not simply a desirable aspect of public utility control facilitating the exercise of commission authority in the direction of lower rates and better service; it is absolutely indispensable if the public is to be assured that the utility will be able to raise adequate capital funds at minimum costs."

The inability of the Commission to control the capital costs of natural gas companies and the capital structure thereof is illustrated by the decision in the El Paso rate case. In a recent opinion pertaining to the El Paso Natural Gas Company, *El Paso Natural Gas Co.*, Opn. No. 366, Docket Nos. G-4769, et al, Opinion and Order Determining Rate of Return and Ordering Rate Filings and Refunds, October 19,

1962) the Commission was confronted with one of the realities which mature from an inability to control the capital costs of natural gas pipeline corporations. Discussing El Paso's capitalization which was created solely by management and with none of the restraints of regulation, the Commission stated:

> "In the present proceeding, the most significant fact with respect to the common equity is that it is so thin . . . A capitalization which reduces overall costs to consumers is to be encouraged provided that it does not go so far as to imperil the financial safety of the company; and the record does not show an immediate danger to El Paso as a result of its thin equity . . ."
>
> "The record indicates that El Paso has a higher debt ratio than any others in a representative group of ten large pipelines and its ratio for common equity is lower than all of the others but one." . . .
>
> "It is not our purpose to encourage any further thinning of the equity but on the contrary we hope our decision will have an opposite effect."

Here is a clear and valid criticism of the capital structure of the world's second largest pipeline corporation, a criticism shared by the financial community, contrary to sound principles of financing, but one, which the Commission was powerless to prevent.

The Federal Power Commission, itself, has long been aware of the deficiencies of the Natural Gas Act. Consistently, it has sought an expansion of its authority and jurisdiction from The Congress, usually without success. By way of example the Thirtieth Annual Report of the Federal Power Commission (1950) relates at page 133:

> "Two bills to amend the Natural Gas Act were introduced during the last fiscal year. One of these, S. 2746, introduced by Senator Johnson of Texas, constituted

a proposal to grant the Commission regulatory authority over the security issues of natural-gas companies similar to that exercised with respect to electric public utilities."

All of the Annual Reports of the Federal Power Commission contain recommendations for amendments to the Natural Gas Act. Recently, the latest Annual Report of the Federal Power Commission (1962) contains an imposing body of recommendations and amendments which bespeak a recognition by the Commission itself of its limitations. (See Appendix A).

In short, over the years the Commission has recommended to the Congress the passage of legislation granting new or additional powers concerning security issues of pipeline companies, abandonment or alienation of properties, collection of information, importation and exportation of gas, direct industrial sales of gas, interconnection of facilities, suspension of rates, hearing procedures, and safety regulations.

As a device to control one of the largest industries in the United States with all of its economic power and the great public dependence upon the commodity it sells, the Natural Gas Act is a thin reed. Its inadequacy is particularly startling when comparison is made with the powers generally given to State regulatory commissions.

The Peculiarities of the Rate-Making Process.

The rate-making process of the Natural Gas Act is a curious device. In operation it inevitably favors the pipeline companies over the consumers. Argument to the contrary cannot erase history. Section 4 of the Natural Gas Act permits the filing of increased rates and charges by a natural gas company and after a thirty-day notice and a five-month

suspension period such rates and charges are permitted to go into effect unless a hearing has commenced. This is totally unlike regulation under the California Public Utilities Code, Section 454, which provides:

> "No public utility shall raise any rate or so alter any classification, contract, practice or rule as to result in any increase in any rate except upon a showing before the Commission and a finding by the Commission that such increase is justified."

Under the Natural Gas Act rates and charges as to pipelines have, over the past years, been made effective without hearing and subject to possible refund. Thus, rates collected grow into mountains of dollars with no determination as to lawfulness leaving the consumer with such protection as an ultimate refund may afford. Some measurement of the shortcomings of the Natural Gas Act in terms of establishing present lawful rates is revealed by that document entitled "Tabulations of Gas Rate Increases to Gas Pipeline Companies as of March 1, 1960. Prepared by the Bureau of Rates and Gas Certificates Federal Power Commission at the request of the House Subcommittee on Legislative Oversight. Dated April 15, 1960." The tabulations there set forth show that as of March 1, 1960, there had been collected the cumulative amount of $506,420,052 subject to refund. From a less authoritative but undoubtedly accurate source comes the information that "as of mid-1962 U.S. pipelines had collected a staggering $1.1 billion subject to refund." (Forbes Magazine, September 1, 1963, The Gas Pipelines: A New Set of Rules? page 20). It is interesting to note that the same publication reports that of the moneys collected subject to refund "one company—El Paso—accounts for about $400 million."

The particular exposure of California, and Texas, New Mexico and Arizona as well, to the rate-making techiniques of the Natural Gas Act are illustrative of the inadequacy of the Natural Gas Act as a rate-fixing device. Set forth in Appendix B herein is the chronology of those rate increase applications pertaining to El Paso. It should be noted that the various dockets and related proceedings referred to by California in Appendix B have been settled and the settlement thereof approved by formal order of the Commission but importantly, this settlement of $155 million by way of refunds and a reduction in the California border price of 3.3¢ per Mcf *was the result of the persistent refusal of California, alone, to accept a lesser figure.*

The findings of the lower Court are grossly erroneous when viewed against the demonstrated weaknesses of the Natural Gas Act. The tale of regulation spun by the trial judge comes from an unawareness of regulation as it is and not as it ought to be.

The history of proceedings under the Natural Gas Act show that pipeline companies partially meet capital requirements through rates and charges exacted from consumers. Refund obligations grow, hearings are deferred, rate increases are pancaked one on top of the other, and consumer interests fight the battle with limited resources handicapped by time and distance from the Commission. The culmination of years of delay and frustration is never a complete success since as this Court pointed out in the Tennessee case, supra, the refund method, for various reasons, is not an adequate remedy. It is a grave thing then in view of the realities of the Natural Gas Act to leave unchecked a pipeline corporation so economically dominant as El Paso was, and as it became, with the acquisition of Pacific.

The Problem of Producer Regulation.

This Court has been exposed to the ages of federal regulation in the evolution toward meaningful producer control. It was thrust upon the Commission in the first instance over its objection in 1954. The Commission has never adopted a consistent method of regulation; instead it has been in a long and seemingly unending period of experimentation. See *Phillips Petroleum Company v. Wisconsin*, 347 U.S. 672 (1954); *Wisconsin v. Federal Power Commission, California v. Federal Power Commission, Long Island Lighting Co. v. Federal Power Commission*, 373 U.S. 294 (1963).

Even the panacea which the latest experiment of area rates is represented to be has begun to show its deficiencies. As recently as November 27, 1963, in Dockets Nos. AR64-1 and AR64-2, Commissioner Ross is strongly critical of the area rate method and spells out his criticism in detail. In disagreeing with his colleagues, Commissioner Ross had these comments as to the area rate method:

> "The tedious and time-consuming approach used in Permian is prohibitive of effective regulation. By the time Permian is decided, it could be stale."

And again:

> "The experience in Permian strongly suggests that the area approach, as presently constituted, and as presently contemplated, is a far cry from being the golden key which will unlock the heretofore undiscovered secrets for successful producer regulation. • • •"

The state of producer regulation is a cross suffered by consumers. And complete consumer protection is only made more difficult by vesting in a single powerful pipeline supplier a priceless position of preeminence over the natural gas markets of the West.

The Wall Against Competition.

El Paso is the giant which supplies natural gas to California. Interestingly enough its pipeline stops at the California border. Its gas is taken at the border by California gas distributing utilities. They in turn resell the product at a utility return to their consumers, firm and interruptibles.

The Los Angeles Basin has long been beset with a smog problem. So grievous has the problem become that local authorities have proscribed the burning of certain materials and particularly the use of fuel oil for most of the year. The world's largest electric utility, Southern California Edison Co., serves in the area below central California. Its demands for energy are enormous but its use of fuel oil is restricted by "smog" ordinances. This means that the Southern California Edison Company, in order to serve its millions of ratepayers, must burn natural gas. It means that Edison, which is under a public utility obligation to render adequate and continuous service at reasonable rates, must have an assured supply of energy.

Accordingly, Edison has made several attempts to obtain for itself its own supply of natural gas. Some years ago it explored the possibility of importing natural gas from Bastian Bay in Louisiana. This project did not materialize.

As the facts recited herein show, it negotiated with Ray Fish of the Pacific Northwest Pipeline Corporation, to obtain natural gas from the Northwest. This possibility was killed after Paul Kayser, President of El Paso, out of concern for his private preserve, flew to California and advised Edison that any arrangements with Pacific Northwest "would not be in the public interest."

Edison thereafter attempted to import gas by a project known as the "Pemex Project" which would bring gas out of Texas into Mexico, thence across to California. This pro-

ject was designed to satisfy the needs of Edison but it was opposed vigorously by El Paso. The extensive hearings in connection with that project made quite clear that the *Edison Company had demonstrated its need for an assured long term annual supply of gas.* The brief of the Public Utilities Commission of the State of California so stated and the record in those proceedings was without contradiction in that regard. Despite the fact, however, of the demonstrated need of Edison, neither El Paso nor the local California gas distributing utilities would meet Edison's needs except upon their arbitrary terms. The Pemex project was subsequently abandoned.

Now both Edison and the Los Angeles Department of Power and Light have entered into a contract with the Gulf Pacific Pipeline Corporation to bring additional gas to Southern California. Edison, the utility, again seeks an assured long-term supply of natural gas. The Los Angeles Department of Power and Light which distributes natural gas to residents within the municipality of Los Angeles also seeks an assured long-term supply of natural gas. This project again is being opposed by El Paso.

El Paso has consistently refused demands of the Edison company. Its position matches neatly the refusal of the gas utilities of Southern California to supply Edison. Edison and the gas utilities of Southern California and thereby El Paso are competitors for the energy markets of Southern California. Thus far, Edison has been unable to break away from dependence upon its gas rivals, and through the unsevered cord which binds Edison and thereby its gas supply, its growth and its service to its chief competitors, it is also tied to El Paso.

There is no authority in law which can compel El Paso to serve natural gas to Edison, except as El Paso elects to do so; and this is particularly grievous if, while withholding

a vital commodity from a California public utility, El Paso also thwarts the efforts of any other suppliers to meet the Edison need. El Paso will serve Edison upon terms El Paso dictates or nobody will serve Edison!

The Natural Gas Act Invites Opposition to Competition.

It is recognized that the Natural Gas Act and the Rules of Practice and Procedure of the Federal Power Commission promulgated thereunder allow easy protest to new certificate applications. Intervention is customarily granted. This means then that any applicant seeking to supply the growing California gas market is always met at the gate by the militant opposition of El Paso. El Paso has opposed every certificate application to California as related. It is expected, of course, that El Paso will quickly reply that the new pipelines of Transwestern Pipeline Corporation and the Pacific Gas Transmission Company serving California since the inception of these proceedings were unopposed by El Paso. Such is the fact but the Court should realize that *these applications for two additional pipelines were made during the pendency of the antitrust action against El Paso.* And it was the very threat of the monopoly complaint which held El Paso to proper restraint and which prevented opposition to those projects. Absent the beneficial and restraining influence of the action of the Department of Justice under Section 7 of the Clayton Act those projects in the opinion of California would not be realities today.

Since the Natural Gas Act permits opposition to new certificates, it is the substance of opposition which should be examined. The El Paso company in opposing new projects avoids a sharing of the future California gas market. That market which El Paso already has is guaranteed by long-term contracts with California utilities and is protected by certificate authority of the Commission.

El Paso in opposing the Gulf Pacific project and other projects blocks the increment in the California market from any other pipeline. The growth of California will require additional pipelines. In the judgment of California it is far better that regulation be accompanied by the salutory incidents which competition alone offers and which is sometimes the best regulator of all.

It should also be realized that in opposing new and additional projects, and particularly those which will benefit so large a state as California, El Paso's opposition is being financed by the ratepayers themselves in the long run. The cost of opposition is neatly covered by that accounting term, "Operating Expenses." The opposition is possible in the first instance because El Paso controls the rich market which is California. El Paso's ratepayers give it the resources to defeat projects, some of which, in the opinion of California, have been in the public interest. These opportunities for opposition exist today and they will exist many times over if this merger is permitted to stand. In the judgment of California, new competitive pipelines are unlikely if this merger stands. The realities of human nature, the great difficulties of putting together sufficient reserves to justify a project; the initial financing, the acquisitions,—all of these things will be the more difficult, if not impossible, if El Paso is absolved of the charges places against it coming from the Clayton Act.

El Paso in the past has exhibited no hesitancy in preventing applicants from obtaining sufficient gas reserves to justify an additional pipeline. When the Transwestern Pipeline Corporation attempted to procure the gas in the Aneth field, in the southwestern portion of the United States, El Paso by continuing higher bids for this new gas took the producer contracts away from Transwestern and the addi-

tional expense and the high price of the new gas was placed into El Paso's system as an operating expense paid for by the consumers. The ratepayer unknowingly pays to destroy competition and the benefits of it.

It is imperative that the expanding gas markets of the West and of California in particular be served with the benefits of competition. Some notion of the unprecedented growth of the natural gas needs of the western United States is set forth by El Paso itself in an advertisement placed by it in newspapers of general circulation and particularly in The Oil Daily, Friday, April 19, 1963:

> "An adequate supply of energy is essential to progress. In the 11 fast-growing western states served by El Paso Natural Gas Company, demand for energy has risen astronomically—as population has soared and the pace of the economy quickened.
>
> "Since 1950, these 11 states have grown 2½ times as rapidly as the rest of the nation. California today is the nation's most populous state. The populations of both Nevada and Arizona have more than doubled. This growth is accelerating year-by-year.
>
> "Vast supplies of energy are needed to meet the mounting demands of these millions of new citizens. And El Paso Natural Gas Company has played a growing role in providing one of the most important sources of this energy.
>
> "Back in 1950, El Paso Natural marketed 295-billion cubic feet of natural gas. By 1962, we were marketing 1.31 *trillion* cubic feet of gas—four and a half times as much as in 1950."
>
> "That's approximately 10 times more energy than is produced each year by all of the federally financed electric power generators, including the giant Bonneville Power Administration and Hoover Dam, in these 11 states."

El Paso overwhelmingly dominates the natural gas markets of the West.

Since these proceedings originally commenced the Transwestern pipeline which follows the route of El Paso's southern system and the Pacific Gas Transmission Company which meanders into California from western Canada have become operational. This is not to say, however, that they present any threat to El Paso and its continued use of its vast economic superiority. The mere existence of an entity in the same industry does not cause meaningful competition. And broadly speaking, El Paso dwarfs the other pipelines as to make competition a myth. El Paso operates a pipeline corporation having a total capitalization in excess of $1 billion. Its revenues in 1962 were in excess of $400 million from a pipeline system more than 10,000 miles in length. Transwestern has a capitalization of approximately $200 million, gross revenues of $47 million from a system 2,400 miles in length. Pacific Gas Transmission has a capitalization of $123 million with revenues of $44 million from a system more than 600 miles in length.

In the hierarchy of pipelines El Paso stands as the "General Motors" and its rivals in lesser positions. These figures demonstrate that their mere existence does not afford that type of competition which the law envisions.

El Paso's Proposals for the Future.

El Paso's plans for continued domination of the California market is evidenced by its proposals to sell additional gas to the California market. The following tabulation covers El Paso's pipeline certificate applications now pending before the Commission indicating the quantities to be delivered and the cost of facilities necessary to accomplish delivery:

FPC Docket No.	Quantities* Firm	Quantities* Excess	New Facility Cost
El Paso CP63-296	60,000,000		None
	40,000,000		$ 3,500,000
El Paso CP64-76	250,000,000 or		$ 50,000,000 or
	575,000,000		$134,000,000

*Cubic feet per day.

Proposals by other pipeline companies for new or additional supplies for the California market are also before the Commission, and El Paso is opposing in whole or in part such certificate applications:

FPC Docket No.	Quantities* Firm	Quantities* Excess	New Facility Cost
Transwestern CP64-34	0	110,000,000	None
Transwestern CP63-204	50,000,000	110,000,000	$ 5,000,000
Transwestern CP64-91	290,000,000		$ 40,000,000
Gulf-Pacific CP63-223	865,000,000		$313,000,000

*Cubic feet per day.

The Judgment of the Lower Court and the Findings and Conclusions in Support Thereof Are Contradicted by the Record.

The findings of the lower court are at war with the realities of the record. Beyond argument Pacific was a real competitor to El Paso. The Pacific pipeline traversed the western states close to California. Pacific had access to supply sources making deliveries to California a possibility. Moreover, it had entered into serious negotiations with the Southern California Edison Company to deliver gas to California. Pacific management was confident of its ability to enter the California market.

But somehow the Trial Judge dismissed Pacific as a competitor.

Why? Evidently because Pacific had not succeeded in its efforts to gain the California market. And, of course, it failed because El Paso acquired and operated Pacific with the management of El Paso, sold Pacific gas at less than cost and, in short, put it into a position of corporate malnutrition.

The result in the trial court furnishes a lesson to one who would be a successful monopolist either by flying trips which block efforts to sell gas to California or by outright stock acquisition. In any event, so long as competition is frustrated, then it follows that never at any time was there competition or the possibility of it.

This is a conclusion totally contrary to the record before the lower court and at variance with those decisions enunciated by this court with reference to Section 7 of the Clayton Act.

The judgment of the lower court and the findings attendant thereon are also explained by the demonstrated insularity of the Trial Judge from the economics of the natural gas industry and the realities of Federal regulation.

Divestiture Should Be Applied Here.

Against an accumulation of advice and warning El Paso pushed its acquisition of Pacific.

As related in the Statement of Facts herein El Paso disregarded the advice of the Attorney General of the United States; the clear warning in the formal complaint of the United States of America herein; the motion of the State of California before the Federal Power Commission seeking to restrain this merger and more recently the language of Justice Douglas in *California v. Federal Power Commission*,

supra, in pointing to the danger of proceeding with a merger that is under attack because of the problem which scrambling creates. El Paso was on notice over and over again that its actions were considered in violation of Section 7 of the Clayton Act. Nonetheless, fully advised of the consequences of an intimate mixture of the affairs of El Paso and Pacific, it proceeded to operate as one corporation.

If the Court construes the evidence below as California does then it should be no defense to complete relief that a hardship will be imposed on El Paso. As this Court stated in *United States v. Dupont*, 366 U.S. 316 at page 326:

"• • • The key to the whole question of an antitrust remedy is of course the discovery of measures effective to restore competition. Courts are not authorized in civil proceedings to punish antitrust violators, and relief must not be punitive. But courts are authorized, indeed required, to decree relief effective to redress the violations, whatever the adverse effect of such a decree on private interests. Divestiture is itself an equitable remedy designed to protect the public interest. In *United States v. Crescent Amusement Co., supra*, where we sustained divestiture provisions against an attack similar to that successfully made below, we said, at p. 189: 'It is said that these provisions are inequitable and harsh income tax wise, that they exceed any reasonable requirement for the prevention of future violations, and that they are therefore punitive. . . . Those who violate the Act may not reap the benefits of their violations and avoid an undoing of their unlawful project on the plea of hardship or inconvenience.'"

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[9]Bills were introduced in the Eighty-sixth Congress to ameliorate the income-tax consequences of gain on disposition of stock pursuant to orders enforcing the antitrust laws. See Hearings on S. 200 before the Senate Committee on Finance, 86th Cong., 1st Sess. (1959); Hearings on H. R. 8126 before the House Committee on Ways and Means, 86th Cong., 1st Sess. (1959); H.R. Rep. No. 1128, 86th Cong., 1st Sess (1959).

"If the Court concludes that other measures will not be effective to redress a violation, and that complete divestiture is a necessary element of effective relief, the Government cannot be denied the latter remedy because economic hardship, however severe, may result. Economic hardship can influence choice only as among two or more effective remedies. If the remedy chosen is not effective, it will not be saved because an effective remedy would entail harsh consequences. This proposition is not novel; it is deeply rooted in antitrust law and has never been successfully challenged.[10] The criteria were announced in one of the earliest cases. In *United States v. American Tobacco Co.*, 221 U.S. 106, 185 (1911), we said:

> 'In considering the subject . . . three dominant influences must guide our action: 1. The duty of giving complete and efficacious effect to the prohibitions of the statutes; 2, the accomplishing of this result with as little injury as possible to the interest of the general public; and, 3, a proper regard for the vast interests of private property which may have become vested in many persons as a result of the acquisition either by way of stock ownership or otherwise of interests in the stock or securities of the combination without any guilty knowledge or intent in any way to become actors or participants in the wrongs which we find to have inspired and dominated the combination from the beginning.'

"The Court concluded in that case that, despite the alleged hardship which would be involved, only dissolution of the combination would be effective, and

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[10] See, e.g., *United States v. Crescent Amusement Co.*, 323 U.S. 173, 189 (1944); *United States v. Corn Products Refining Co.*, 234 F. 964, 1018 (D.C.S.D.N.Y. 1916), appeal dismissed on motion of appellant, 249 U.S. 621 (1919); *United States v. E. I. du Pont de Nemours & Co.*, 188 F. 127, 153 (C. C. D. Del. 1911), modified, 273 F. 869 (D.C.D. Del. 1921); *In re Crown Zellerbach Corp.*, CCH Trade Reg. Rep. 1957-1958 ¶ 26,923, at p. 36,462 (F. T. C. 1958).

therefore ordered dissolution. Plainly, if the relief is not effective, there is no occasion to consider the third criterion."

CONCLUSION

This case is best understood by applying basic concepts. A monopoly as here is controlled by a business concern which makes it possible to fix the prices and regulate the output of a commodity and a service. As concerns prices, this monopoly, in view of the easy virtue of Section 4 of the Natural Gas Act, has the power to fix the price of natural gas by arbitrary methods sanctioned by federal law. Federal regulation is not designed to control a pipeline monopoly. Competition should be preserved. And remembering that the government below had merely to demonstrate that this merger *might substantially lessen competition or tend to create a monopoly*, it seems clear that the government's case has been made.

WILLIAM BENNETT
Special Counsel for the State of California

(Appendices follow)

Appendix A

LEGISLATIVE RECOMMENDATIONS

The Commission during the past year has made an extensive review of its existing statutory authority under the Federal Power Act and the Natural Gas Act. In the light of that review and experience gained during this period, we have drafted a legislative program designed to enable us to carry out more effectively the policies which the Congress has entrusted to this Commission.

Fifteen specific recommendations are being made to the Congress and the President, two of which are included in our proposed legislative program for the first time. Two of the items proposed in our 1961 Annual Report were enacted into law, while four others have been dropped from our legislative recommendations this year.

New Recommendations

The two new recommendations included for the first time this year are:

1. *Acquisition of controlling interest in natural gas pipline companies.*—Amend section 7(c) of the Natural Gas Act to require a certificate of public convenience and necessity for the acquisition of the controlling interest in a natural gas pipeline company, and to provide that the grant of a certificate authorizing the acquisition of either a controlling stock interest or the assets of such a natural gas pipeline shall relieve the transaction from liability under the antitrust laws.

Section 7(c) now provides that Commission approval must be secured for the acquisition by any person of the assets of a natural gas pipeline company. In *California v. Federal Power Commission*, 369 U.S. 482 (1962), the Supreme Court held that the Commission's authority does not

extend to approval of acquisitions of controlling stock interests in natural gas pipeline companies and that, contrary to the situation now prevalent with respect to other Federal regulatory agencies possessing power to approve acquisitions, approval by the Commission of an acquisition does not exempt the transaction from subsequent prosecution under the antitrust laws. The Commission believes that where an industry is subject to the detailed regulation which it now exercises with respect to the operations of the interstate pipelines, it is essential that the Commission also have authority to pass upon stock acquisitions affecting control of the pipelines. We also believe that, with respect to all acquisitions, stock or asset, the Commission should have the responsibility for determining the extent to which competition would or would not serve the public interest, with its approval of any transaction having the effect of immunizing it from prosecution under the antitrust laws.

2. *Licensing of steam-electric plant facilities on navigable waters.*—Amend the Federal Power Act to provide for Commission licensing of new facilities to be erected in or abutting the navigable waters of the United States for the diversion of water for use in a steam-electric generating plant.

At present the Commission's licensing jurisdiction under Part I of the Federal Power Act is limited to projects for the generation of hydroelectric power. But increasingly in recent years plants for steam-electric generation have been built adjacent to navigable waters of the United States with diversion facilities in, across or along the stream to provide water for cooling purposes. Under existing law such projects have required special authorizing legislation by the Congress. It is believed that the determinations of the relationship of such projects to the comprehensive devel-

opment of navigable waters of the United States can efficiently and promptly be made by this Agency, which has performed this function with respect to hydroelectric projects since 1920, while relieving Congress of an increasingly burdensome task. In recognition of the more limited control which need be exercised over facilities located on navigable waters in connection with steam-electric plants, the amendment spells out the limits of Commission authority.

Recommendations Which Are Being Renewed

Amendments to the Natural Gas Act

3. *Broadened informational authority.*—Amend section 14(a) so as to give the Commission broad powers to conduct investigations and collect information with respect to the natural gas industry similar to those now conferred on it with respect to the electric industry by section 311 of the Federal Power Act.

This would fill a serious void in the Commission's effectiveness for, in the absence of authority such as is presently provided for the electric power industry by the provisions of section 311 of the Federal Power Act, the existing statistical information on the industry as a whole is inadequate to meet the needs for detailed industry information of value to the Commission, Congress, other Government agencies, and the general public. As in the case of the analogous section of the Federal Power Act, the proposal makes clear that the new informational activities would not subject to the Commission's jurisdiction any persons not already subject thereto, nor would the proposal call for information otherwise available from industry sources. This proposal was expressly endorsed in President Kennedy's special message of March 14, 1962, relating to additional protection of the consumer interests of the nation.

4. *Regulation of security issues of pipeline companies.*—Amend section 12 of the Natural Gas Act to give the Commission jurisdiction with respect to the security issues of natural gas pipeline companies which are subject to the act.

The Commission regards control over the security issues of the interstate pipelines, whose rates and services are subject to its jurisdiction, as important from the standpoint of maintaining the strength and stability of these companies. The high rate of growth gives added urgency to this recommendation. The proposal in form follows the language in the Federal Power Act giving the Commission authority over the securities of certain power companies, but the scope of Commission authority has been somewhat broadened in view of the fact that the Commission exercises direct control over a much larger percentage of the business of the interstate pipelines than is the case with respect to most power companies.

5. *Abandonment or alienation of services, facilities or reserves.*—Amend the abandonment section 7(b): (*a*) to require Commission approval for the disposition by an interstate natural gas pipeline company of gas reserves which in whole or part have constituted the basis for the issuance of certificates of public convenience and necessity; (*b*) to substitute notice and opportunity for hearing for the present mandatory hearing requirement; and (*c*) to make it clear that Commission approval is required for abandonment of certificated sales as well as for the abandonment of service and facilities.

Of these three interrelated proposals, the first is the most important. Our experience shows that it is difficult if not impossible adequately to regulate pipeline production of gas if a pipeline company may freely alienate vast gas reserves it has accumulated (often at the expense of its ratepayers),

and upon which certification of extensive facilities may have been based. Yet the decision of the Supreme Court in *F.P.C. v. Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, prior to the time it was determined that the Commission had jurisdiction over the price at which gas is sold by producers for resale in interstate commerce, casts doubt upon the Commission's ability to deal with the problem directly and efficiently.

The proposed abolition of the mandatory hearing requirement stems from our experience indicating that many abandonment requests are routine and unopposed. A formal hearing in such cases merely takes time and requires diversion of needed manpower.

The other proposal, in order to avoid claims which have occasionally been made that an application under the subsection is required only when jurisdictional facilities are to be abandoned, makes explicit that Commission approval is required before any certificated sale may be abandoned.

6. *Additional authority as to the importation and exportation of natural gas.*—Amend sections 1(b) and 2 so as to give the Commission the same control over the transportation and sale of natural gas in foreign commerce as it now has over transportation and sales in interstate commerce.

Section 1 of the act declares that the Federal regulation of the sale and transportation of natural gas in *both* interstate and foreign commerce is necessary in the public interest. However, the decision in *Border Pipe Line Co. v. F.P.C.*, 172 F.2d 149, held that the Commission has no ratemaking or certification jurisdiction over a company exporting or importing natural gas from or to a State adjacent to the international border, although a limited degree of control over the export or import of gas is provided under section 3 of the act. Absence of control over such gas coextensive

with that provided for gas sold or transported in interstate commerce leaves a significant gap in the regulatory scheme which should be remedied. This is particularly true in the face of the increasing production of gas in Canada and Mexico.

7. *Direct sales for industrial use.*—Amend section 1(b) so as to vest jurisdiction in the Commission over direct interstate sales by natural gas pipeline companies for industrial use. Conforming amendments to sections 1(c) and 2(6) would be necessary to effect this proposal.

This proposal would enhance the Commission's ability to cope with the problems of undue discrimination, prejudice, and preference. Ratemaking procedures would be simplified and expedited by doing away with the necessity of allocating costs between interstate sales for resale now subject to our jurisdiction and direct sales in interstate commerce. It would also eliminate much of the pipeline's incentive to make unregulated sales which have frequently resulted in a diversion of gas for inferior uses.

8. *Compulsory and emergency interconnections.*—Amend section 7 by adding a new subsection giving the Commission authority, on its motion or upon complaint, to order pipeline companies to interconnect with and serve one another, after notice and opportunity for hearing and a finding that such interconnection or service is necessary or appropriate in the public interest. In cases of emergency the Commission would be given authority to order temporary interconnection and service without a hearing and, when essential to national security, to allocate the supply of gas.

The Commission now has limited authority under section 7(a) of the act to direct a natural gas company to interconnect with and sell gas to a local distributing company, but since interconnections of the pipeline systems themselves,

like those involving electric power pools, can greatly assist in the distribution of available supplies to the points where they are most needed, we believe the Commission's authority should be broadened as proposed. As in the case of section 7(a), the Commission's authority to order permanent interconnections would be exercised only where it can find that its action will place no undue burden upon the natural gas pipeline company, require no enlargement or undue extension of its mainline facilities, and does not impair its ability to render adequate service to its existing customers.

9. *Extension of suspension period.*—Amend section 4(e) to authorize the Commission, in its discretion, to extend the time of suspension of a proposed change in a currently effective rate schedule for a further period not exceeding 3 months beyond the 5-month period for which it may be suspended under the existing provisions of the subsection.

This is a modification of a recommendation we made last year when we suggested that the Commission be authorized to extend the suspension period for 6 additional months. The shorter period is now recommended because, while we do not believe we can hope to complete a major pipeline rate case within the 5-month period now provided after suspension, the major revision of our procedures for trying pipeline rate cases within the last year leads us to believe that an 8-month period is a realistic goal. We would not expect to invoke any discretion given us to extend the 5-month statutory suspension period for producer rate filings pending conclusion of area rate proceedings, except possibly in those cases where an increased rate establishing a new plateau in a given area is set for immediate hearing, to avoid the adverse effects upon the industry rate structure generally of permitting such rates to go into effect.

10. *Notice and opportunity for hearing in certificate cases.*—Amend section 7(c) to eliminate the mandatory hearing requirement, substituting in lieu thereof a provision for due notice and opportunity for hearing.

As noted above with respect to the abandonment provision in section 7(b), there are many cases in which neither the interest of the parties nor the public welfare requires that a formal hearing be held, and to do so only causes unnecessary delay. A hearing would be held when protests by interested parties raising substantial factual issues are received or when the Commission deems a hearing necessary in the public interest.

11. *Safety regulations.*—Amend section 7 by the addition of a new subsection authorizing the Commission to prescribe safety regulations with respect to the construction and operation of interstate natural gas pipelines.

While the industry in general is doing a good job in this respect, the lack of any Federal regulation, and the scattered and nonuniform State regulation, cannot be considered entirely satisfactory. High-pressure interstate pipelines necessarily present elements of hazard, and at least in the absence of adequate and uniform State laws every practicable step should be taken by the Federal Government to protect the public from inherent dangers.

Appendix B

CHRONOLOGY OF G-4769

October 14, 1954	El Paso filed for increased rates.
November 15, 1954	Rates suspended by Commission order.
April 15, 1955	El Paso puts rates into effect.
July 11, 1956	Hearings commenced.
December 12, 1956	Hearings concluded.
March 20, 1958	Presiding Examiner's decision.
July 8-9, 1958	Oral argument.
August 10, 1959	Commission decision issued.
September 8, 1959	Application for Rehearing.
October 8, 1959	Order Denying Application for Rehearing.
August 2, 1960	Order of remand by this Court.
September 30, 1960	Rehearing denied by this Court.
May 1, 1961	Certiorari denied.
July 24, 1961	New hearings commence.
October 19, 1962	New decision issued.
December 4, 1963	Case settled.

CHRONOLOGY OF G-12948

June 28, 1957	El Paso filed for increased rates.
July 26, 1957	Rates suspended by Commission order.
January 1, 1958	El Paso puts rates into effect.
July 24, 1961	Consolidated hearings commence.
October 19, 1962	Interim decision issued.
December 4, 1963	Case settled.

CHRONOLOGY OF G-17929

January 12, 1959	El Paso filed for increased rates.
February 27, 1959	Rates suspended by Commission order.
August 1, 1959	El Paso puts rates into effect.

July 24, 1961.....Consolidated hearings commence.
October 19, 1962.....Interim decision issued.
December 4, 1963.....Case settled.

CHRONOLOGY OF RP60-3

February 23, 1960.....El Paso filed for increased rates.
March 23, 1960.....Rates suspended by Commission order.
August 25, 1960.....El Paso puts rates into effect.
July 24, 1961.....Consolidated hearings commence.
October 19, 1962.....Interim decision issued.
December 4, 1963.....Case settled.